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R. J. REYNOLDS TOBACCO COMPANY 1968 ANNUAL REPORT

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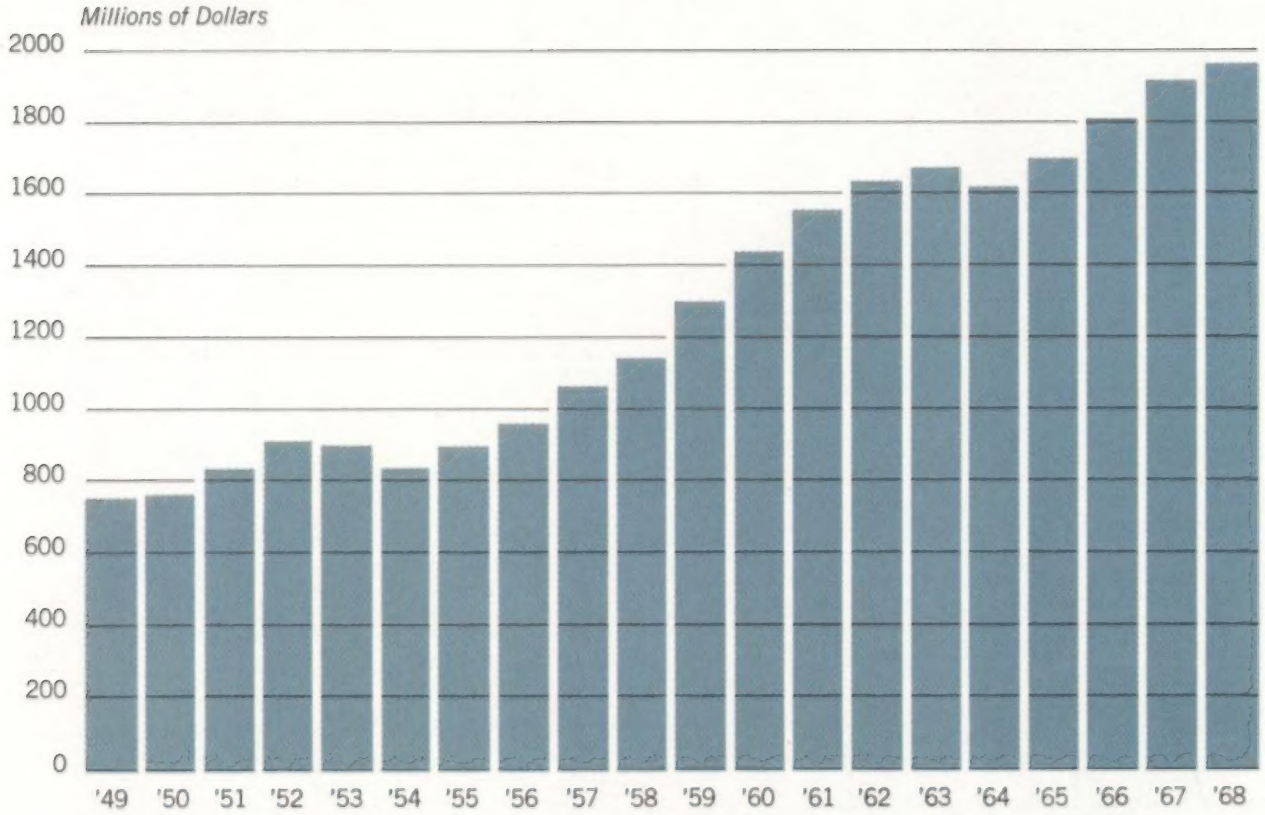
Comparative Summary

CONSOLIDATED

TWENTY YEAR SALES

Millions of Dollars



	1968	1967
Net sales	$1,962,487,755	$1,911,414,209
Net earnings	150,044,830	150,952,208
Per share of Common Stock*	3.71	3.73
Net earnings as a percentage of net sales	7.65%	7.90%
Dividends on Preferred Stock	$ 720,000	$ 720,000
Dividends on Common Stock	88,518,214	82,283,651
Per share of Common Stock	2.20	2.05
*Based on average number of shares outstanding	40,235,552	40,302,863
Capital expenditures	$ 24,127,108	$ 31,536,041
Depreciation	26,172,774	26,601,836
Total assets	$ 1,197,107,385	$1,243,521,934
Current assets	881,591,017	924,749,306
Current liabilities	224,498,227	324,719,392
Net current assets—working capital	657,092,790	600,029,914
Real estate, machinery and equipment—net	206,528,662	209,686,877
Long-term debt	34,000,000	41,000,000
Equity of holders of Preferred Stock	20,000,000	20,000,000
Equity of holders of Common Stock	918,609,158	857,802,542
Number of stockholders at year end	136,129	134,038
Number of regular employees at year end	21,332	21,127

BOWMAN GRAY

A. H. GALLOWAY

To the Stockholders

The sales of your Company on a consolidated basis reached a new high in 1968 and pre-tax earnings also set a record. Dividend payments on Common Stock increased for the fifteenth consecutive year and were the highest in the Company's history.

Consolidated sales were $1,962,487,755, up 2.7%. Pre-tax earnings were $326,613,830, an increase of 7.2% over those of the previous year. However, the 10% Federal income tax surcharge held 1968 net earnings to $150,044,830, compared with $150,952,208 in 1967.

The Company continued to lead the U.S. tobacco industry in both domestic and export cigarette sales. While the Company's domestic sales were off slightly, its export sales increased, and total cigarette sales in 1968 exceeded the record set in 1967.

Three R. J. Reynolds brands—WINSTON, SALEM and CAMEL—were among the four best-selling cigarettes in the United States, and they continued to lead all other brands in their categories in 1968 sales volume. Also during the year, WINSTON strengthened its position as the No. 1 cigarette brand in the nation.

Export cigarette sales increased for the twelfth consecutive year as the Company enlarged its share of the export business and maintained its position of leadership as the largest exporter of cigarettes from the United States.

The Company's international tobacco operations were further consolidated during the year with the formation in September of R. J. Reynolds International. This new division is responsible for international production and marketing of Reynolds' consumer products in Central and South America, the Pacific, Australia, New Zealand, and the Far East. R. J. Reynolds (Europe) S.A., with headquarters in Geneva, continues to be responsible for production and marketing of Reynolds' consumer products in Europe, the Middle East, and Africa.

Plans for increasing the Company's share of the tobacco business in the growing foreign markets are being accelerated, and this expansion program should make good progress in many overseas areas during the coming year.

The growth of the tobacco industry in the United States continues to be adversely affected as a result of the increasingly exorbitant state cigarette taxes and the effects of the punitive actions and propaganda attacks engendered by the smoking and health controversy.

Despite claims of anti-smoking forces, no new evidence was introduced in 1968 to support the contention that cigarettes are causative of human disease. In July, The Committee for Research on Tobacco and Health of the American Medical Association reported that "the problems related to establishing any kind of cause and effect relationship between tobacco use and health are far more complex than had been supposed." At the fifteenth annual meeting of The Council for Tobacco Research–USA in January, 1969, Dr. Clarence Cook Little, Scientific Director of the Council, said: "There is no demonstrated causal relationship between smoking and any disease. The gaps in knowledge are so great that those who dogmatically assert otherwise –whether they state that there is or is not such a causal relationship– are premature in judgment. If anything, the pure biological evidence is pointing away from, not toward, the causal hypothesis."

The Company, and others in the industry, are continuing their dedi-

cated efforts to support independent scientific research to learn the truth concerning the smoking and health issue and to fill the gaps in knowledge that exist. We hope that in 1969 government and private health research agencies will also accelerate their efforts to achieve this goal. It is also hoped that the industry will not be subjected to further restrictions based solely upon statistical assumptions and medically unsupported claims.

With respect to the Company's non-tobacco business, planned programs for orderly growth in food and beverages, aluminum sheet and foil, packaging, and corn products proceeded on schedule. In general, considering the prevailing trends in their respective industries, the subsidiaries made good progress during the year.

R. J. Reynolds Foods, Inc., made excellent gains, and sales and profits were ahead of those for 1967. Archer Products, Inc., increased its sales, and 1968 was a profitable year for each of its three operating divisions. Filmco, Inc., maintained sales volume in its highly competitive industry, but dollar sales and profits were lower due to pricing conditions. Penick & Ford's sales declined for the first time in ten years due to a prolonged strike. This, coupled with unsatisfactory pricing in the corn refining industry, caused Penick & Ford to have a loss in its operations in 1968.

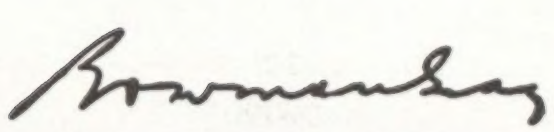
Further increases in productive capacity for both tobacco and non-tobacco products were made in 1968. Capital expenditures totaled $24,127,000. For 1969 it is estimated that additional investments for construction and further expansion and modernization of plant installations and equipment will approximate $25,000,000.

The new Development Center in Winston-Salem, completed in 1968, is now fulfilling an important function for the Company and its subsidiaries in developing new products and improving existing ones. This facility should play an increasingly significant role in future growth.

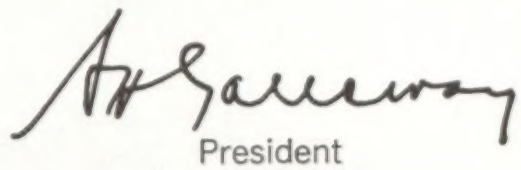
A major step in the Company's continuing diversification program was taken with the announcement in January, 1969, of plans to acquire McLean Industries, Inc., which, through its subsidiaries, operates the largest containerized freight service system in the world. Our stockholders were advised of this by letter dated January 17. Agreement has been reached on financial terms, and, subject to completion of investigation and agreement on other important matters, we hope to submit the proposal to our share owners for approval at the forthcoming annual meeting.

On behalf of the Board of Directors and our entire management, we acknowledge the individual contributions of our 21,000 employees, whose loyalty and dedication make it possible for our Company to progress. We also appreciate the loyalty and support of the 136,000 stockholders and their interest in the growth of the Company.

Respectfully submitted for the Board of Directors.



Chairman, Board of Directors



President

February 6,1969

Research and Product Development

The Company's new Development Center, dedicated in October, 1968, brought into existence a unified program of combining modern research and development procedures for the creation of new products. In this Center, ideas from the market place, from operations and from scientists and engineers are blended together into concepts of new products and improvements of existing products. Prototypes are made and tested by the development and marketing people to determine the commercial potential. If the tests indicate acceptability by the consumer, the new product is then launched in the market place.

The Research Department is responsible for the acquisition of fundamental information. Over the years, extensive scientific research has led to an increasing knowledge of the composition of tobacco, tobacco smoke, and filtration of tobacco smoke. This research has been instrumental in the development of existing Reynolds brands which have been so successful.

The Company's basic research is not confined to tobacco products. Considerable research has been in progress for many years in other areas of the business, such as foods, starches, and packaging. More recently the Company has expanded its research into other fields, and the department is staffed to assist in the over-all diversification program.

The new Development Center is the most modern in the industry, and its scope and versatility make it one of the most efficient facilities of its kind now in operation. The multi-building Center contains the laboratories, full-size pilot plants, and administrative offices of Reynolds' Product Development and Mechanical Development Departments. Both departments now serve the Company's tobacco operations as well as the subsidiary operations of R. J. Reynolds Foods, Archer Products, Penick & Ford, and Filmco.

The Product Development Department is organized into four divisions —Tobacco Products, Food Products, Package Development, and Product Evaluation—and a Special Services staff.

Using the new laboratory and pilot plant facilities, the department's tobacco products staff can simulate every manufacturing operation involving cigarettes and cigarette filters, tobacco processing, and leaf processing. In the Center's modern kitchens, food experts can prepare and test food products under actual home conditions. Food production techniques can be developed under simulated manufacturing conditions in the food pilot plant. The package development staff has equipment for developing and testing new and existing materials for Archer Products and Filmco.

The Mechanical Development Department, with its new facilities, has become another avenue of Company diversification, licensing inventions and innovations to U. S. and foreign equipment manufacturers.

At the dedication ceremony, President Galloway said: "This Development Center is destined to play a most significant role in the progress of the R. J. Reynolds Tobacco Company. Today our corporation has no choice but to look as far into the future as possible and—in terms of developing the products and processes to keep our Company going—even work in the future. It is this facility that will house a group of highly skilled people who are spending their time working in the future, so that when tomorrow comes our total organization will be prepared to offer what the consumer needs and wants."

RJR Tobacco Products

In 1968 R. J. Reynolds Tobacco Company maintained its leadership as the largest producer of cigarettes in the United States for both the domestic and the export markets.

Total cigarette sales by the Company again increased, with a gain in export shipments offsetting a slight decline in domestic volume.

Three Reynolds brands—WINSTON, SALEM, and CAMEL—were among the four best-selling cigarettes in the domestic market, and each continued as the leader in its category.

WINSTON further widened its lead in 1968 over its closest rival as the No. 1 brand in the industry. King Size WINSTON again was the largest-selling 85-millimeter brand, and WINSTON Super King was the top seller among all 100-millimeter brands.

For the eleventh consecutive year, SALEM was the leading menthol cigarette. In the 100-millimeter menthol category SALEM Super King led all others.

CAMEL continued to hold its dominant position among regular-size, non-filter cigarettes, accounting for well over half of the sales of such cigarettes. CAMEL Filter again made an important contribution.

Although not a major brand, TEMPO continued to be marketed as the Company's entry in the charcoal-filter category.

DORAL, a new cigarette combining a unique filter system with flavorful tobaccos, was placed in an Oregon test-market in early November. Results of the test were so successful that expansion into other test markets followed in January, 1969. DORAL, in both regular and menthol versions, was created to meet the demands of smokers who want a flavorful cigarette with low "tar" and nicotine content.

The volume of the Company's smoking tobacco sales was off slightly from that of the previous year. PRINCE ALBERT maintained its position as the nation's best-selling smoking tobacco, and CARTER HALL continued to show growth. DAYS WORK remained in top place in sales of all plug chewing tobacco brands.

Effective advertising in a wide variety of media contributed to Reynolds' continued sales leadership in tobacco products in 1968.

All of the Company's major cigarette brands were broadly promoted in the mass media of network and spot television, network and spot radio, general magazines, and men's, women's, and farm magazines. Supplementary advertising weight was provided by point-of-sale display materials, Railway Express truck posters, and transportation car cards.

The major smoking tobaccos also were given strong advertising support: PRINCE ALBERT in network television, spot radio, and farm magazines; CARTER HALL in network television sports programs; and MADEIRA MIXTURE in national magazines.

In December a $7,000,000 expansion program for the Company's Whitaker Park cigarette plant was initiated, to be completed by the spring of 1970. Additional space will be used for tobacco blending, tobacco processing, shipping, and material storage. The expansion will provide for current production requirements plus room for growth to meet increased demands.

This program is further evidence of the Company's determination to remain the nation's leading manufacturer of cigarettes and its faith in the continued success of the entire tobacco economy.

International Operations

Another step in the Company's program of international expansion was the formation in September, 1968, of R. J. Reynolds International. This new division, based in Winston-Salem, further consolidates the Company's international tobacco operations in large areas of the world. It is also responsible for expanding international production and marketing of food items in such areas.

Responsibility for the Company's operations in Europe, the Middle East, and Africa remains under R. J. Reynolds (Europe) S.A., headquartered in Geneva, Switzerland. The European operation is aggressively pursuing the development of markets for Reynolds Foods' products in Europe.

Sales of the Company's cigarette brands in Europe, including those exported from the United States as well as those manufactured in Europe, were greater than in 1967. Manufacture of WINSTON Super Kings was begun in Germany and Switzerland. Substantial gains in sales of Reynolds brands were accomplished by manufacturing licensees in Austria and Holland.

For the twelfth consecutive year, Reynolds cigarette brands gained in export sales, with the Company retaining its leadership as the largest exporter of cigarettes from the United States and increasing its share of this business.

Reynolds' leading position in the important Puerto Rican market was strengthened, with significant growth in both sales and share of market. Through the Company's interest in Fabrica de Cigarros Baloyan, S.A., of Mexico, SALEM was firmly established on a national basis in the fast-growing Mexican market and WINSTON was put into test-marketing. As a result of the licensing arrangement in effect in Peru, WINSTON sales showed a gain in that country.

Promotional activities at overseas military bases were stepped up, with sales of the Company's cigarette brands increasing substantially.

Because of the potential in foreign markets, the new International Division is planning market expansion in other areas of the free world.

R. J. REYNOLDS INTERNATIONAL Winston-Salem, N.C. H. E. RICHMILLER, *President*

TABACALERA NACIONAL, S.A. (Licensee)
Lima, Peru

FABRICA de CIGARROS BALOYAN, S.A.
Tijuana, Mexico
SIRAK M. BALOYAN, *President*

R. J. REYNOLDS (Europe) S.A. Geneva, Switzerland JACQUES E. BORIN, *President*

REYNOLDS CIGARETTE CORPORATION
Aarau, Switzerland
MAURICE PERRET, *Manager*

REYNOLDS-NEUERBURG G.m.b.H.
Cologne, West Germany
DR. HANS BÜHLER, *General Manager*

AUSTRIA TABAKWERKE, A.G. (Licensee)
Vienna, Austria

THEODORUS NIEMEYER, N.V. (Licensee)
Groningen, Holland

GLENN TOBACCO COMPANY Athens, Greece EDWIN M. LEIGHT, *Manager*

R. J. Reynolds Foods, Inc., the Company's wholly-owned subsidiary for foods and beverages, recorded growth in sales and profits in 1968.

Five Reynolds Foods' lines continued in top position in their respective categories in 1968. CHUN KING Oriental foods, PATIO Mexican foods, and HAWAIIAN PUNCH South Pacific beverages, Reynolds' line of "international" foods, maintained their leadership and achieved a high rate of growth. Also retaining the No. 1 rank in their fields were COLLEGE INN chicken specialties and BRER RABBIT molasses and syrups—domestic products with substantial use as ingredients.

MY-T-FINE desserts and VERMONT MAID syrups, with intensive in-store promotion to complement advertising support, achieved increased volume. MY-T-FINE instant puddings, which were made available to new markets throughout the country, did particularly well.

New products marketed by Reynolds Foods in 1968 included: VERMONT MAID pure maple and maple-walnut syrups; Maple-y-Cane BRER RABBIT syrup; three varieties of egg rolls—chicken, lobster, and shrimp—in the frozen CHUN KING line; sliced and diced canned chicken in the COLLEGE INN group; "Taste of Pineapple" in HAWAIIAN PUNCH; and frozen burritos in the PATIO Mexican line.

It is expected that several new products within each brand category will be test-marketed and introduced during 1969. The facilities of the Company's new Development Center will be of great assistance in creating new food items of consistently high quality to meet consumer desires as well as in improving present products.

Food and Beverage Products

BJR FOODS

Production was substantially increased in the Jackson, Ohio CHUN KING plant in 1968 with the installation of new freezing equipment. Additional capacities are planned for other food products.

Emphasis will continue to be placed on specialty convenience products with advantages that can be promoted to the consumer through advertising. Promotion was increased last year for all Reynolds Foods' brands, with advertising on television and radio, in newspapers and magazines, and at the point-of-purchase.

Contributing to Reynolds Foods' growth was increased efficiency in marketing and manufacturing operations, stemming from careful planning and budgetary control.

R. J. REYNOLDS FOODS, INC. · 750 Third Avenue, New York, N.Y.
JOHN PHILLIPS, *President*
Plant Locations: Addison, Illinois · Atlanta, Georgia · Baltimore, Maryland · Burlington, Vermont
Cambridge, Maryland · Duluth, Minnesota · Fullerton, California · Harvey, Louisiana
Hoboken, New Jersey · Jackson, Ohio · Kahului, Maui, Hawaii · Lockport, New York
Pinckneyville, Illinois · Plymouth, Indiana · San Antonio, Texas · San Juan, Puerto Rico
Ste. Therese, Quebec · Windsor, Ontario

Industrial Corn Products

The growth pattern of Penick & Ford, Limited, which for more than ten years had set annual records in volume of corn products sold, was interrupted by an 87-day work stoppage. This strike by the local union, plus continued price-cutting in the industry, caused the subsidiary to operate below expected levels, resulting in lower sales and a net loss for the year.

Despite the labor difficulties, which have been settled, the subsidiary completed projects approved in prior years to increase the production capacity of its Cedar Rapids plant. These expanded facilities, strategically located in the heart of the Midwestern corn belt, will enable Penick & Ford to meet the demands of growing markets.

Penick & Ford produces a large number of grades of corn starch, including many specialty types. These are sold to a broad spectrum of industrial users, such as food producers, confectioners, the paper and textile industries, and chemical manufacturers. Among the other corn derivatives produced are syrups, oils, gums, dextrines, refined grits, gluten feed, and gluten meal.

In converting corn starch into various types of syrups, the characteristics are modified to meet customers' needs. These syrups are used by bakers, confectioners, ice cream manufacturers, packers of jams, jellies, and preserves, and fruit and vegetable canners. The food processing industry's utilization of highly specialized corn sweeteners is increasing.

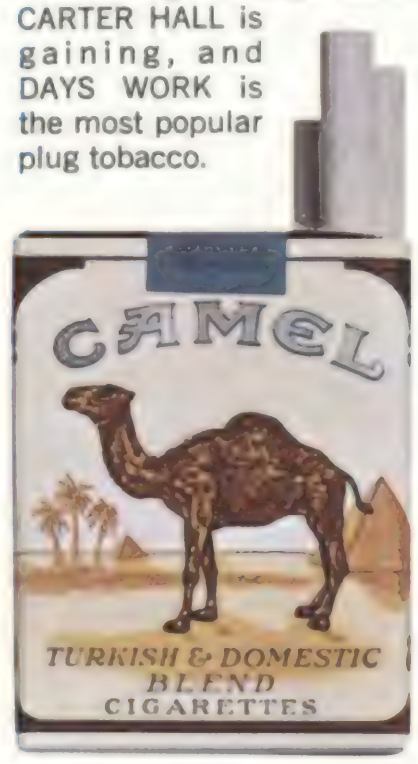
The Potato Products Division operated at a satisfactory level during the year.

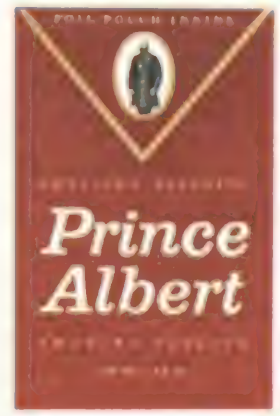
Extensive efforts are continuing in research and development in the corn refining area, looking forward to wider usage of corn derivatives and broader profit margins.

PENICK & FORD, LIMITED · Cedar Rapids, Iowa
R. V. CRONIN, *President*
Plant Locations: Aberdeen, Idaho · Blackfoot, Idaho · Cedar Rapids, Iowa · Idaho Falls, Idaho
Monte Vista, Colorado

RJR TOBACCO BRANDS
Industry Leaders

Three of the four top U. S. cigarette brands are RJR products. WINSTON, No. 1, outsells all others. SALEM is the top menthol brand, CAMEL the leading regular-size. PRINCE ALBERT is the best-selling smoking tobacco. CARTER HALL is gaining, and DAYS WORK is the most popular plug tobacco.





Chocolate
MY*T*FINE®
Pudding & Pie Filling
4 half-cup servings... NET WT. 3-5/8 OZ
Brer Rabbit
Real New Orleans
MOLASSES
GET 25¢ FREE
CHUN KING
12 MEAT & SHRIMP EGG ROLLS

FOOD AND BEVERAGE PRODUCTS

Market Leaders

Five Reynolds food brands hold top market positions: CHUN KING Oriental foods, HAWAIIAN PUNCH, BRER RABBIT molasses and syrups, COLLEGE INN chicken specialties, and PATIO Mexican foods. MY-T-FINE desserts and VERMONT MAID syrups are also very popular brands.

ALUMINUM AND PACKAGING PRODUCTS

ARCHER PRODUCTS, INC., is a leading producer of colorful flexible packaging materials in paper, aluminum foil, and plastic combinations. Industrial aluminum sheet and foil are manufactured to exacting tolerances and various gauges and alloys. For consumers, Archer makes gift wrap and household and florist foils. FILMCO supplies grocers with protective vinyl wraps for meat and produce, also *Bishrink* vinyl wraps for industrial packagers.

Aluminum and Packaging Products

Archer Products, Inc., completing its second year of operations as a subsidiary, made substantial gains in 1968. All three divisions operated profitably and had sales gains in excess of their respective industry growth rates.

Operating five plants employing more than 1,000 persons, Archer Products, Inc., has established a broad and firm base on which to expand. Additional support for its growth is provided by the Company's new Development Center.

Increased capacity and broader capabilities made possible by the new aluminum sheet and foil rolling plant at Huntingdon, Tennessee, enabled the *Metals Division* to penetrate new industrial markets. Significant progress was made in sales of litho sheet, which is used to make plates for offset printing. Archer is now one of the major suppliers for this industry. The line of products serving the electrical industry continued to expand, particularly conductor strip for use in transformers.

The Metals Division is one of the nation's leading producers of light-gauge aluminum foils. It is a major supplier of specialty aluminum and foil to the electrical, building, packaging, and air conditioning and heating industries for a wide variety of end-uses.

Aluminum foil produced by the Metals Division is used by Archer's own Packaging Division, as well as by outside customers, to produce packaging materials of laminated foil, paper, board, and plastic films. It is also used by the Consumer Products Division for household and florist foils and gift wraps.

The *Packaging Division,* expanding its facilities and improving its technology, further increased its sales of flexible packaging materials in 1968 to producers of dried and prepared foods, refrigerated and frozen foods, and other consumer non-durable and durable products.

Among the division's products are foil and paperboard cartons, printed labels and liner stock for canisters, printed package inner wraps and overwraps, labels, colored and printed free foil, printed and unprinted polyethylene combinations with or without foil, and plastic film combinations. With its technical and production skills Archer can solve both marketing and functional packaging problems from initial design to finished product.

Archer materials are used by some of the largest packaged goods companies in the world to package a wide variety of foods, pharmaceuticals, beverage concentrates, and other consumer household products.

The *Consumer Products Division* broadened its product lines during the year, and increased its manufacturing capacity at Greeneville, Tennessee.

The division continued to be the nation's leading producer of florist foils. In 1968 it also moved into the top five suppliers of Christmas gift wraps, which are sold under private labels and Archer's own "Gay Note" and "Archer" brand names. Major department stores, variety chains, grocery chains, and retail drug outlets carry these products.

The division's household foils are also marketed under the "Gay Note" brand name as well as under a growing number of private labels for major grocery chains and other retail outlets.

ARCHER PRODUCTS, INC. · Winston-Salem, North Carolina
SAMUEL A. ANGOTTI, *President*
Plant Locations: Greeneville, Tennessee · Huntingdon, Tennessee
Winston-Salem, North Carolina

Vinyl Packaging Products

Filmco
PACKAGING FILMS

Filmco, Inc., which supplies vinyl packaging films to food stores as protective wraps for meat and produce, recorded 1968 volume about the same as in the previous year. Dollar sales and profits, however, declined because of lower prices in the industry.

Current development programs are expected to provide additional opportunities to further the use of vinyl films for non-food packaging uses.

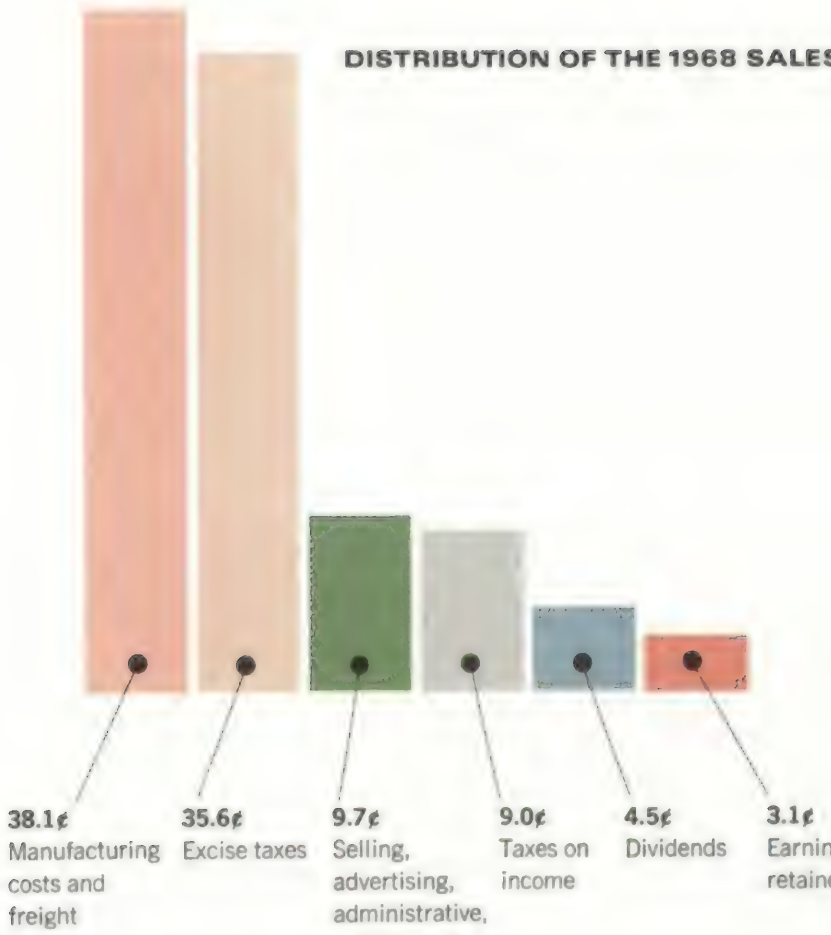
Filmco International faced the same problem encountered in Filmco's domestic operations—price competition—which held sales to about the same dollar value as in the previous year. Production facilities of this subsidiary in Sedgefield, England, which became operational in late 1967, are now running near capacity. Plans are under way to increase capacity in 1969.

Filmco International sells polyvinyl packaging films for food and non-food packaging applications in most Western European countries as well as in Peru, Venezuela, Mexico, South Africa, and the Caribbean area. Arrangements have been completed for distribution in Japan.

In March, Filmco International was presented the President's "E" Award for Exports, in recognition of "an outstanding contribution to the export expansion program of the United States of America."

FILMCO, INC. · Aurora, Ohio
PAUL J. VAUGHAN, *President*
Plant Locations: Aurora, Ohio · Sedgefield, England

DISTRIBUTION OF THE 1968 SALES DOLLAR

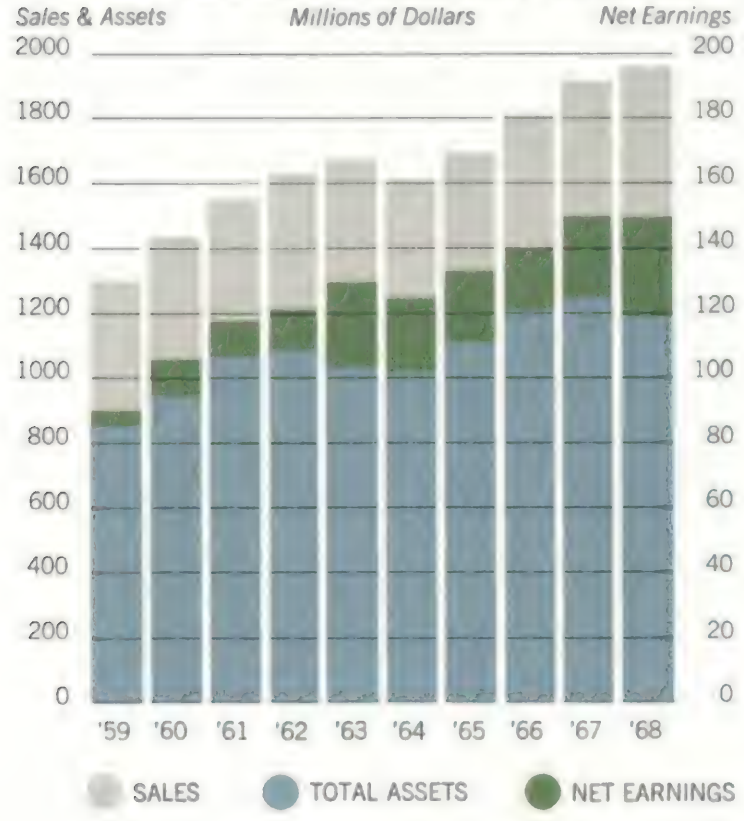


38.1¢	35.6¢	9.7¢	9.0¢	4.5¢	3.1¢
Manufacturing costs and freight	Excise taxes	Selling, advertising, administrative, and interest expenses	Taxes on income	Dividends	Earnings retained

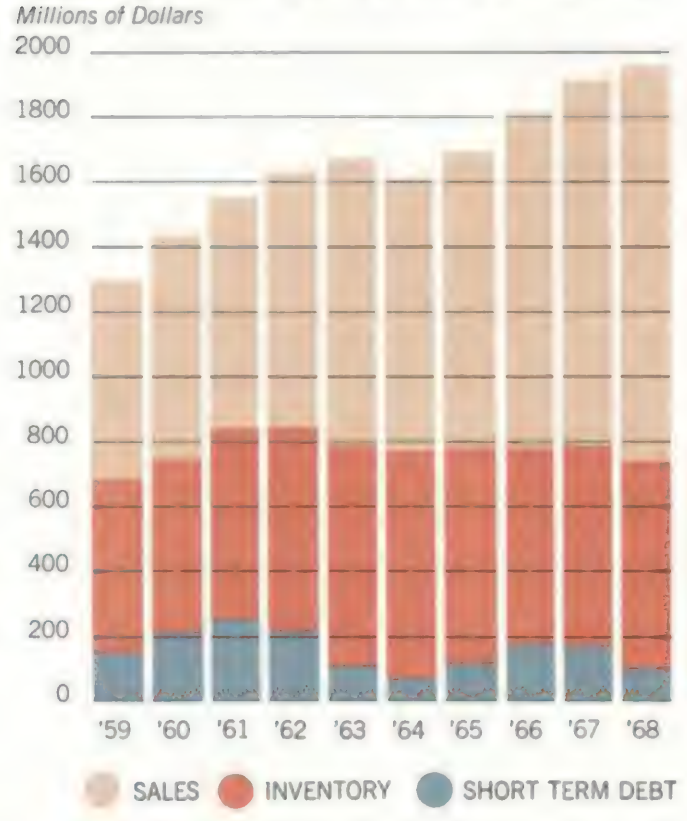
SOURCE AND DISPOSITION OF CORPORATE FUNDS

SOURCE		DISPOSITION	
Net earnings	$150,044,830	$ 89,238,214	Dividends paid
		Increase in working capital	
		100,221,165	Decrease in current liabilities
		43,158,289	Less: Decrease in current assets
		$ 57,062,876	
Depreciation	26,172,774	24,127,108	Expenditures for expansion and modernization
Other	1,210,594	7,000,000	Decrease in long-term debt
Total	$177,428,198	$177,428,198	Total

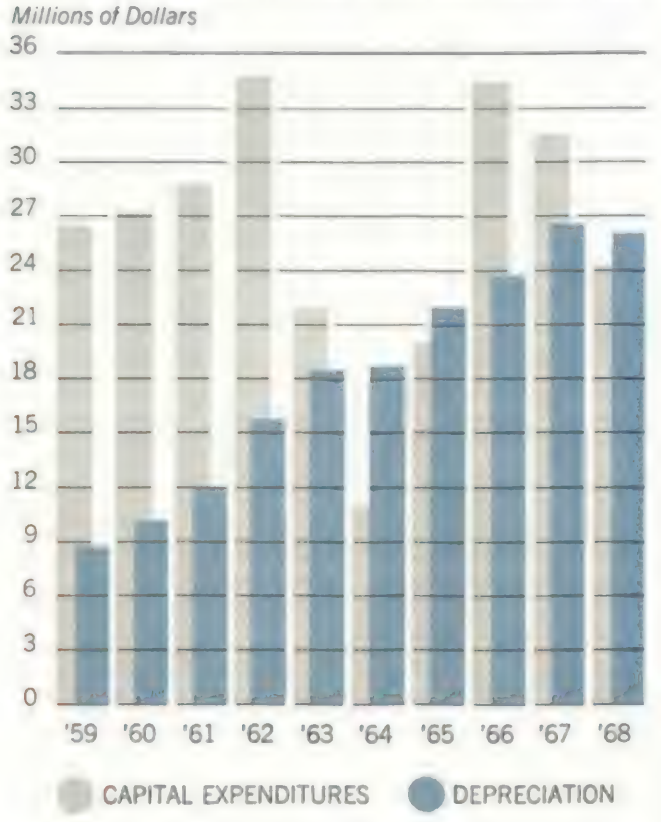
SALES, TOTAL ASSETS AND NET EARNINGS



SALES, INVENTORY AND SHORT TERM DEBT



CAPITAL EXPENDITURES AND DEPRECIATION



Financial Review 1968

Sales

Sales during 1968 of $1,962,487,755 were the highest in the history of the Company, exceeding the 1967 record of $1,911,414,209 by 2.7%. Record sales were achieved in both tobacco and food activities.

Sales of tobacco products, which include $697,806,366 of excise taxes, accounted for 88% of consolidated sales.

Earnings

Earnings before provision for income taxes climbed $21,874,622 to $326,613,830 in 1968, a 7.2% increase over the $304,739,208 in 1967. Contributing to the increase were higher sales, continuing production efficiencies, and lower interest charges. However, net earnings of $150,044,830 during 1968 were 0.6% lower than the previous year's record of $150,952,208 due to the 10% surcharge on Federal income taxes which reduced net earnings by $14,880,904 or 37 cents per share. Net earnings per share of Common Stock, after the effect of the surcharge, were $3.71 compared with $3.73 the year before.

Dividends

For the fifteenth consecutive year, dividend payments on the Common Stock increased, totaling $2.20 per share in 1968. Dividends paid during the year aggregated $89,238,214, the highest for the Company's sixty-nine years of consecutive dividend payments.

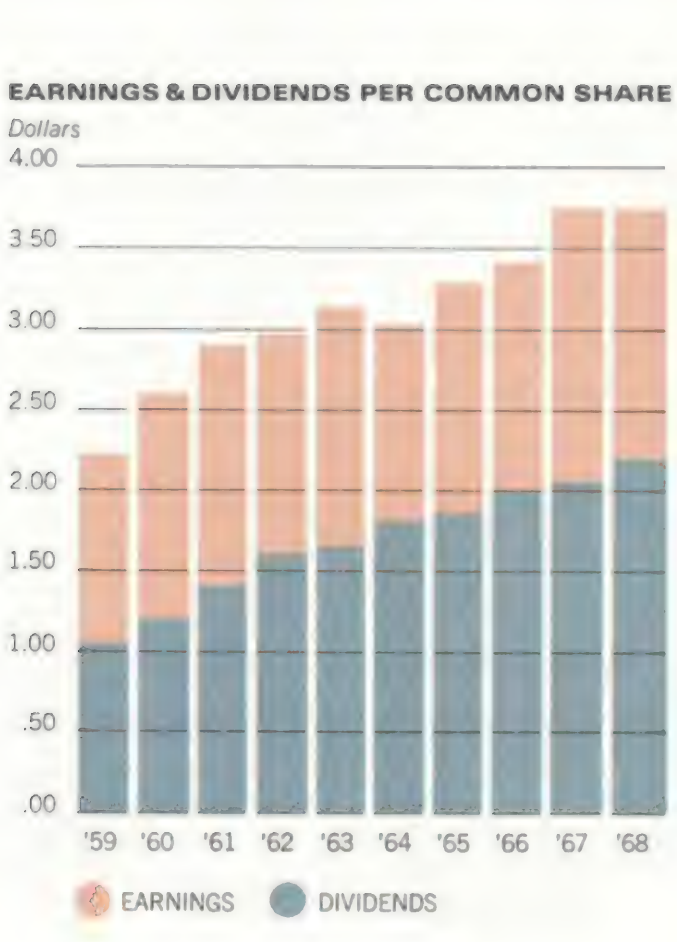
Debt Position

Short-term debt on December 31, 1968, was $107,500,000, or $68,000,000 less than at the close of business in 1967. The Company was completely free of short-term debt for a short period in September. Long-term debt was $34,000,000 at year end, a reduction of $7,000,000 during the year.

Capital Expenditures

Capital expenditures in 1968 totaled $24,127,108. The largest single project was the completion of the $9,000,000 Development Center in Winston-Salem. Substantial outlays were also made for modernizing cigarette manufacturing and leaf processing facilities. Approximately $7,000,000, or 29% of capital expenditures, was invested in expansion and modernization of installations engaged in non-tobacco activities. Capital expenditures for 1969 are currently estimated at $25,000,000. Plans include continued expansion of food processing capacity and a $7,000,000 expansion of the modern Whitaker Park cigarette manufacturing facility in Winston-Salem.

EARNINGS & DIVIDENDS PER COMMON SHARE



Ten Year Summary

(Dollar amounts in thousands, except share statistics)

Year ended December 31,	1968	1967	1966
SALES, EARNINGS AND DIVIDENDS			
Net sales	$1,962,488	$1,911,414	$1,804,199
Earnings before taxes on income	326,614	304,739	278,994
Federal and state taxes on income	176,569	153,787	138,999
Net earnings	150,045	150,952	139,995
Dividends on Preferred Stock	720	720	720
Dividends on Common Stock	88,518	82,284	79,825
FINANCIAL POSITION AND EQUITIES			
Working capital	$ 657,093	$ 600,030	$ 558,161
Current assets:			
Inventories	752,254	797,059	791,803
Other current assets	129,337	127,690	116,914
Total current assets	881,591	924,749	908,717
Plant and equipment—net	206,529	209,687	204,225
Other non-current assets	108,987	109,086	100,988
Total assets	1,197,107	1,243,522	1,213,930
Current liabilities:			
Short-term debt	107,500	175,500	180,650
Current maturities of long-term debt	2,000	3,005	4,080
Federal and state income tax liabilities	42,432	44,426	66,351
Other current liabilities	72,566	101,788	99,475
Total current liabilities	224,498	324,719	350,556
Long-term debt	34,000	41,000	48,000
Equity of holders of Preferred Stock	20,000	20,000	20,000
Equity of holders of Common Stock	918,609	857,803	795,374
STATISTICAL INFORMATION			
Capital expenditures	$ 24,127	$ 31,536	$ 34,548
Depreciation	26,173	26,602	23,641
Per common share			
Net earnings *	3.71	3.73	3.41
Dividends	2.20	2.05	2.00
Book value	22.83	21.32	19.70
*Based on average number of shares outstanding (Adjusted for 2-for-1 splits in 1961 and 1959)	40,235,552	40,302,863	40,800,745
Number of RJR shareholders at year end	136,129	134,038	131,371

1965	1964	1963	1962	1961	1960	1959
$1,693,148	$1,613,802	$1,672,445	$1,627,541	$1,555,527	$1,438,547	$1,306,197
266,376	251,725	277,601	260,977	265,220	224,018	199,825
133,019	127,720	148,535	139,821	146,499	117,643	108,507
133,357	124,005	129,066	121,156	118,721	106,375	91,318
722	768	858	936	1,044	1,135	1,296
75,006	73,734	67,602	64,512	56,439	48,345	42,260
$ 608,287	$ 665,030	$ 620,120	$ 568,413	$ 542,047	$ 499,782	$ 480,112
783,434	775,282	795,565	845,929	845,185	745,125	686,324
98,224	91,908	82,551	84,317	84,590	82,099	73,710
881,658	867,190	878,116	930,246	929,775	827,224	760,034
181,633	144,361	150,023	147,568	129,001	112,606	96,153
48,696	7,651	9,501	11,313	9,085	13,926	3,199
1,111,987	1,019,202	1,037,640	1,089,127	1,067,861	953,756	859,386
125,000	67,000	114,500	222,350	258,556	216,639	158,422
6,400	5,396	5,700	6,000	6,000	6,000	6,000
77,431	82,422	96,304	89,605	92,939	77,633	78,173
64,540	47,342	41,492	43,878	30,233	27,170	37,327
273,371	202,160	257,996	361,833	387,728	327,442	279,922
55,000	62,000	68,000	74,000	80,000	86,000	92,000
20,000	20,272	22,459	24,974	27,871	29,511	34,301
763,616	734,770	689,185	628,320	572,262	510,803	453,163
$ 20,246	$ 11,085	$ 21,940	$ 34,727	$ 28,747	$ 27,072	$ 26,491
21,859	18,583	18,339	15,648	12,039	10,241	8,888
3.27	3.01	3.13	2.94	2.87	2.57	2.20
1.85	1.80	1.65	1.60	1.40	1.20	1.05
19.00	17.98	16.82	15.34	13.97	12.47	11.07
40,528,050	40,968,611	40,964,177	40,957,619	40,957,106	40,951,641	40,944,537
118,281	114,010	103,282	97,383	89,550	81,856	81,063

Consolidated Balance Sheets

DECEMBER 31, 1968 AND 1967

ASSETS	1968	1967
Current assets:		
Cash	$ 30,210,990	$ 29,266,571
Marketable securities—at cost (approximately equal to market)	—	300,214
Accounts receivable (less discounts)	97,201,247	94,718,000
Leaf tobacco, supplies, manufactured products, etc.—at cost (substantially all on last-in, first-out basis)	752,254,471	797,059,253
Prepaid expenses	1,924,309	3,405,268
Total current assets	881,591,017	924,749,306
Real estate, machinery and equipment—at cost		
Land and land improvements	11,982,407	11,494,031
Buildings and leasehold improvements	114,286,053	104,539,214
Machinery and equipment	257,508,491	241,509,705
Construction in process	11,892,981	19,983,627
	395,669,932	377,526,577
Less allowances for depreciation	189,141,270	167,839,700
Net real estate, machinery and equipment	206,528,662	209,686,877
Investments in and advances to unconsolidated foreign subsidiaries	18,071,681	17,875,110
Cost in excess of net assets of businesses acquired	84,736,742	84,736,742
Brands, trade-marks and good will	1	1
Other assets	6,179,282	6,473,898
	$1,197,107,385	$1,243,521,934

See notes to financial statements.

LIABILITIES AND STOCKHOLDERS' EQUITY	1968	1967
Current liabilities:		
Notes payable	$ 107,500,000	$ 175,500,000
Accounts payable and sundry accrued accounts	72,565,655	101,788,409
Portion of long-term debt due within one year (less principal amount of debentures in treasury—$5,000,000 in 1968; $3,995,000 in 1967)	2,000,000	3,005,000
Federal and state income taxes	42,432,572	44,425,983
Total current liabilities	224,498,227	324,719,392
Long-term debt (due annually 1970-1972, $7,000,000; 1973, $13,000,000):		
2½% Promissory Note	6,000,000	8,000,000
3% Debentures, due October 1, 1973	28,000,000	33,000,000
Total long-term debt	34,000,000	41,000,000
Stockholders' equity:		
Preferred Stock—par $100 Authorized and issued 490,000 shares, 3.60% Series	49,000,000	49,000,000
Common Stock—par $5 Authorized—60,000,000 shares; issued—40,971,533 shares	204,857,665	204,857,665
	253,857,665	253,857,665
Earnings retained	739,139,683	678,333,067
	992,997,348	932,190,732
Less cost of stock in treasury:		
Preferred Stock, 3.60% Series (290,000 shares)	24,571,415	24,571,415
Common Stock (735,981 shares)	29,816,775	29,816,775
	54,388,190	54,388,190
Total stockholders' equity	938,609,158	877,802,542
	$1,197,107,385	$1,243,521,934

Statement of Earnings

FOR THE YEARS ENDED DECEMBER 31, 1968 AND 1967

	1968	1967
Net sales	$1,962,487,755	$1,911,414,209
Costs and expenses:		
Cost of products sold	1,445,785,281	1,423,264,981
Selling, advertising, general and administrative expenses	182,507,421	172,947,969
Interest and debt expense	7,581,223	10,462,051
	1,635,873,925	1,606,675,001
Earnings before provision for taxes	326,613,830	304,739,208
Provision for Federal and state taxes on income	176,569,000	153,787,000
Net earnings	$ 150,044,830	$ 150,952,208
Net earnings per share of Common Stock	$3.71	$3.73

Statement of Earnings Retained

FOR THE YEARS ENDED DECEMBER 31, 1968 AND 1967

	1968	1967
Earnings retained at beginning of year	$ 678,333,067	$ 610,384,510
Add net earnings	150,044,830	150,952,208
	828,377,897	761,336,718
Deduct:		
Cash dividends—		
Preferred Stock, 3.60% Series	720,000	720,000
Common Stock at $2.20 per share for 1968 ($2.05 per share for 1967)	88,518,214	82,283,651
	89,238,214	83,003,651
Earnings retained at end of year	$ 739,139,683	$ 678,333,067

See notes to financial statements.

Notes to Financial Statements

NOTE A—Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its domestic and Canadian subsidiaries. All intercompany items and transactions have been eliminated in consolidation. Accounts of other foreign subsidiaries are not consolidated, such investments being carried at equity.

The Company is not amortizing the cost in excess of the net assets of businesses acquired.

NOTE B—Depreciation

During the year depreciation charged against earnings totaled $26,172,774, compared with $26,601,836 during 1967. Substantially all assets acquired after 1953 are depreciated using an accelerated method of depreciation; assets acquired prior thereto are depreciated using the straight-line method.

NOTE C—Pension Plans

The Company and its consolidated subsidiaries have several pension plans covering substantially all employees. The total pension expense for the year was $3,017,714, compared with $2,771,495 in 1967, of which the major portion applied to a plan funded under the aggregate cost method. The Company's policy is to fund pension cost accrued. The total amount of assets so funded exceeded the actuarially computed value of vested benefits according to the most recent actuarial valuation.

NOTE D—Penick & Ford

There is pending in the United States District Court for the District of New Jersey an action brought by the United States of America against the Company to require the divestiture of the assets and business it acquired in June 1965 from Penick & Ford, Ltd., Incorporated. The Company is contesting this action.

NOTE E—Subsequent Event—
McLean Industries, Inc.

On January 10, 1969, the presidents of the Company and of McLean Industries, Inc., reached an agreement in principle on a plan whereby the Company would acquire all or a portion of the common stock of McLean Industries, Inc. Under the terms of this plan the McLean shareholders would be offered for each McLean common share $50 cash or, at their option, $40 principal amount of 20-year, 7 percent, subordinated debentures of the Company and ⅝ of a warrant to purchase one share of the Company's common stock at $47.50, such warrant to be exercisable at any time within a 15-year period. The debentures would be non-callable for 10 years but could be used in lieu of cash upon exercise of the warrants. While agreement was reached on these financial terms, other important matters remain to be investigated and agreed upon. The plan is subject to the approval of the directors and common shareholders of the Company and, depending on the final form of the plan, may be subject to approval by the directors and shareholders of McLean Industries, Inc. At year end 1968 there were 10,632,000 shares of McLean Industries, Inc. common stock outstanding and stock options outstanding for an additional 225,800 shares.

Report of Independent Accountants

R. J. Reynolds Tobacco Company, its Directors and Stockholders

We have examined the consolidated financial statements of R. J. Reynolds Tobacco Company and consolidated subsidiaries for the year ended December 31, 1968. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the accompanying balance sheet and statements of earnings and of earnings retained present fairly the financial position of R. J. Reynolds Tobacco Company and consolidated subsidiaries at December 31, 1968, and the results of their operations for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year. It is also our opinion that the statement of source and disposition of corporate funds for the year ended December 31, 1968, shown on page 20 presents fairly the information shown therein.

Ernst & Ernst

Winston-Salem, N. C., February 6, 1969.

BOARD OF DIRECTORS

A. H. GALLOWAY
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GORDON GRAY
REUBEN P. HUGHES
WILLIAM R. LYBROOK
THRUSTON B. MORTON
CHARLES F. MYERS, JR.
DAVID S. PEOPLES
H. H. RAMM
FENTON D. ROYSTER
JOSEPH H. SHERRILL
W. S. SMITH, JR.
J. PAUL STICHT
COLIN STOKES
CHAS. B. WADE, JR.

OFFICERS

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Chairman, Board of Directors

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President and Chairman, Executive Committee

COLIN STOKES
Executive Vice President

DAVID S. PEOPLES
Executive Vice President

W. S. SMITH, JR.
Executive Vice President

H. H. RAMM
Vice President and General Counsel

CHAS. B. WADE, JR.
Vice President

WILLIAM R. LYBROOK
Vice President and Secretary

JOSEPH H. SHERRILL
Vice President

FENTON D. ROYSTER
Vice President

WM. D. HOBBS
Vice President

C. H. JUDGE
Vice President

C. F. BENBOW
Treasurer

W. S. GRANT
Comptroller

RJR

R. J. Reynolds Tobacco Company
Winston-Salem / North Carolina

REGISTRAR

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350 Park Avenue
New York, New York 10022

TRANSFER AGENTS

THE CHASE MANHATTAN BANK, N.A.
1 Chase Manhattan Plaza
New York, New York 10015

FIRST JERSEY NATIONAL BANK
1 Exchange Place
Jersey City, New Jersey 07303

R. J. Reynolds Tobacco Company · Winston-Salem · North Carolina